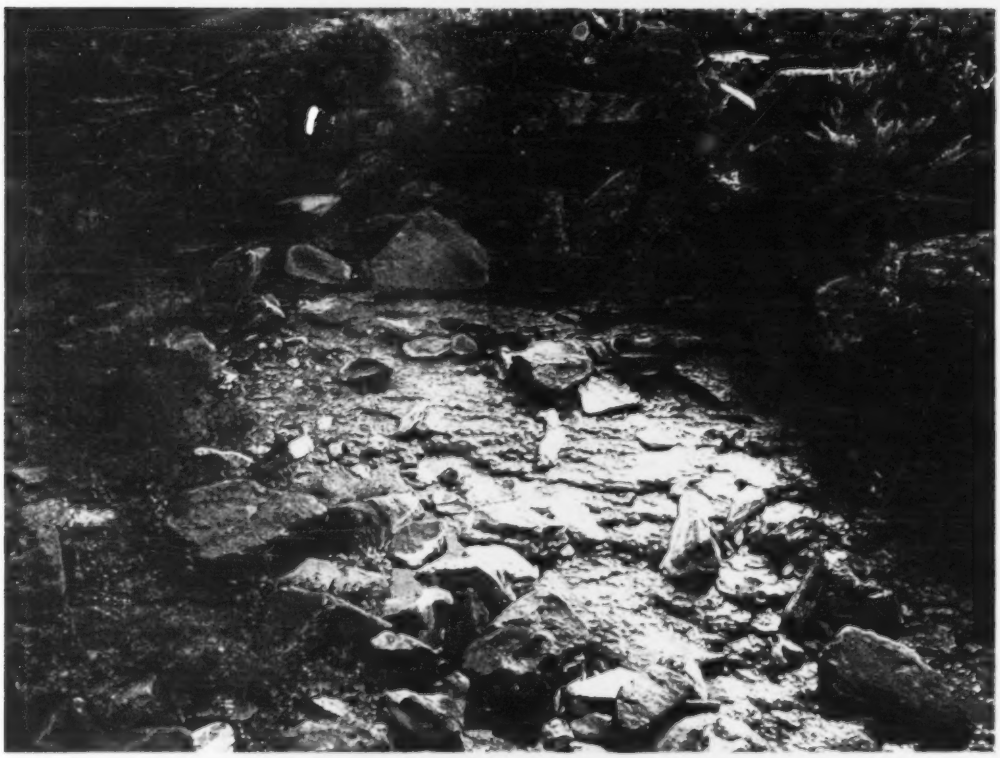
Yukon Development Corporation
2009 Annual Report



Yukon Development Corporation

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Message from the Chief Executive Officer

The Yukon Development Corporation (YDC) 2009 annual report was prepared under our Board's direction and represents a balanced and accurate summary of the Corporation's performance for the calendar year ending December 31, 2009.

2009 was a particularly challenging year for both our employees and Board of Directors. The board chair, along with three directors, resigned in June. Three new board members were appointed in October.

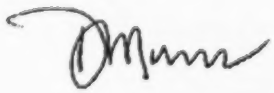
In 2009, the Yukon Development Corporation worked toward securing a $100-million dollar bond issuance. Negotiations to secure this funding continue throughout the year and should be concluded in 2010. They money will be used to help finance some of Yukon Energy Corporation's major projects, including Mayo B and Stage 2 of the Carmacks-Stewart Transmission Line.

Mayo B will increase the ability to generate renewable power from five megawatts to approximately 15 megawatts without the need for a new dam. The project will offset greenhouse gas emissions by approximately 25,000 tonnes a year. Carmacks-Stewart Stage 2 will connect Yukon's two established hydro-based transmission grids and allow Yukon Energy to manage its assets as one inter-connected system.

Also this year, the Tr'ondek Hwech'in First Nation made an investment in Yukon Energy's Mayo- Dawson transmission line of $5 million. YDC is pleased to have the First Nation as a partner in this project.

In 2009, the Yukon Development Corporation provided approximately $1.2 million for the Yukon government's Rate Stabilization Fund (RSF). The RSF was a subsidy provided to non-government residential, commercial and municipal customers as a measure to protect customers from significant bill increases that would have resulted from the shutdown of the Faro mine. The Yukon government ended the subsidy on June 30, 2009, replacing it with the Interim Energy Rebate Program, aimed at assisting residential customers. The Yukon Development Corporation provided $1.4 million for this program in 2009, the full amount of which will be re-imbursed to YDC by the Yukon government.

In close, I would like to take the opportunity to thank the Yukon Development Corporation Board of Directors for their continued commitment, wisdom and guidance, and the YDC staff for their hard work and professionalism.



David Morrison
Chief Executive Officer

Organizational Overview

Yukon Development Corporation (YDC) is a crown corporation created in 1986 by the *Yukon Development Corporation Act*. We are governed by a Board of Directors appointed by the Yukon government and have a legislative mandate to participate with the private sector in the economic development of the Yukon. In particular, the Act mandates the corporation to:

- Develop and promote the development of Yukon resources on an economic and efficient basis;
- Promote employment and business opportunities for territorial residents;
- Assure a continuing and adequate supply of energy in a manner consistent with sustainable development; and
- Implement development policy directives issued to it by the Yukon Cabinet.

Order-in-Council 1993/07 restricted the corporation's role to energy-related activities designed to promote the economic development of the Yukon, and to:

- Assure a continuing and adequate supply of energy;
- Alleviate the effects of any energy shortage that may occur; and
- Promote the establishment, development and operation within the Yukon of industries or undertakings that are by their nature energy-dependent through the provision of cost-effective energy or energy-related infrastructure.

Board of Directors

Board members to June 2009:

Willard Phelps (Chair)
Martin Allen
Paul Birckel
Greg Hakonson
Paul Hunter
Pat Irvin
Barb Joe
Luke Johnson

Board members as of October 2009:

Ray Hayes (Chair)
Paul Birckel
Kevin Brewer
Pat Irvin

Barb Joe
Luke Johnson
Erik Nyland

Board of Directors' Appointments
The Board of the Yukon Development Corporation is appointed by the Yukon government.

Honoraria
Remuneration for Yukon Development Corporation board members is based on Category D of the published Government of Yukon rates for Boards and Committees.
As stipulated in Order in Council 2004/214, the Board Chair's remuneration is capped at $38,000 per year.

Board members receive $100 per half day meeting, and $200 per full day meeting. They do not receive any remuneration for meeting prep time.

Senior Management

David Morrison, Chief Executive Officer

Shelley Dixon, Corporate Secretary

Yukon Development Corporation

Consolidated Financial Statements

December 31, 2009

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Yukon Development Corporation

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

The consolidated financial statements of Yukon Development Corporation are the responsibility of management, and have been prepared in accordance with Canadian generally accepted accounting principles consistently applied and appropriate in the circumstances. The preparation of financial statements necessarily involves the use of estimates and approximations, which have been made using careful judgement. In management's opinion, the consolidated financial statements have been properly prepared within reasonable limits of materiality and within the framework of the accounting policies summarized in the consolidated financial statements.

Management maintains systems of internal controls designed to provide reasonable assurance that assets are safeguarded and that reliable financial information is available on a timely basis. These systems include formal written policies and procedures, the careful selection and training of qualified personnel, and an organizational structure that provides for the appropriate delegation of authority and segregation of responsibilities.

The financial statements have been examined by an independent external auditor. The external auditor's responsibility is to express an opinion on whether the consolidated financial statements, in all material respects, fairly present the Corporation's financial position, results of operations and cash flows in accordance with Canadian generally accepted accounting principles. In addition, the external auditor reports on whether proper books of account have been kept by the Corporation, the consolidated financial statements are in agreement therewith, and the transactions coming to their notice have, in all significant respects, been in accordance with specified authorities. The Auditor's Report, which follows, outlines the scope of this examination and the auditor's opinion.

The Corporation's Board of Directors, through its Audit and Finance Committee, oversees management's responsibilities for financial reporting. The Audit and Finance Committee meets with management and the independent external auditor to discuss auditing and financial matters, to gain assurance that management is carrying out its responsibilities and to review and approve the consolidated financial statements. The auditor has full and free access to the Audit and Finance Committee, with and without the presence of management.

David Morrison
Chief Executive Officer

Blaine Anderson, C.A.
Chief Financial Officer

Whitehorse, Yukon
March 12, 2010

Auditor General of Canada
Vérificatrice générale du Canada

AUDITOR'S REPORT

To the Minister Responsible for the Yukon Development Corporation

I have audited the consolidated balance sheet of Yukon Development Corporation as at December 31, 2009 and the consolidated statements of operations, comprehensive income and retained earnings and cash flows for the year then ended. These financial statements are the responsibility of the Corporation's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with Canadian generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Corporation as at December 31, 2009 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles. As required by the *Yukon Development Corporation Act*, I report that, in my opinion, these principles have been applied on a basis consistent with that of the preceding year.

Further, in my opinion, proper books of account have been kept by the Corporation and by its wholly-owned subsidiary and the consolidated financial statements are in agreement therewith. In addition, the transactions of the Corporation and of its wholly-owned subsidiary that have come to my notice during my audit of the consolidated financial statements have, in all significant respects, been in accordance with the *Financial Administration Act* of Yukon and regulations, the *Yukon Development Corporation Act* and regulations, the *Public Utilities Act* and regulations, the *Business Corporations Act*, and the articles and bylaws of the Corporation and its wholly-owned subsidiary.

Sheila Fraser

Sheila Fraser, FCA
Auditor General of Canada

Vancouver, Canada
March 12, 2010

Yukon Development Corporation

Consolidated Balance Sheet

As at December 31, (in thousands of dollars)	2009	2008
Assets		
Current assets		
Cash	$ 17,167	$ 686
Accounts receivable (note 5)	9,180	5,291
Materials and supplies	2,758	2,566
Prepaid expenses	394	278
Current portion of direct financing leases (note 8)	760	682
	30,259	9,503
Energy infrastructure fund (note 6)	-	760
Customer contribution financing (note 7)	17,424	14,991
Direct financing leases (note 8)	575	1,335
Property, plant and equipment (note 9)	206,507	193,477
Diesel contingency fund (note 10)	887	883
Deferred uninsured losses (note 11)	111	556
Deferred charges (note 12)	13,506	10,673
	$ 269,269	$ 232,178
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities (note 13)	$ 6,668	$ 8,568
Construction financing (note 14)	25,000	-
Derivative related liability (note 25)	296	1,397
Current portion of long-term debt (note 16)	4,059	3,738
	36,023	13,703
Faro Mine dewatering deferral revenue (note 15)	397	1,191
Long-term pension liability (note 22)	1,036	801
Energy Infrastructure Fund (note 6)	-	760
Long-term debt (note 16)	30,926	29,936
Contributions in aid of construction (note 17)	46,258	39,959
Regulatory provision for future removal and site restoration costs	5,008	5,168
Diesel contingency fund (note 10)	887	883
	120,535	92,401
Equity		
Contributed capital	41,501	41,501
Retained earnings	107,233	98,276
	148,734	139,777
	$ 269,269	$ 232,178

Commitments and Contingencies (notes 23 and 24)
The accompanying notes are an integral part of the financial statements.

Approved by the Board:

Chair Director

Yukon Development Corporation

Consolidated Statement of Operations, Comprehensive Income and Retained Earnings

For the year ended December 31, (in thousands of dollars)	2009	2008
Revenue		
Sales of power (note 18)	$ 31,321	$ 28,311
Government of Yukon - Interim electrical rebate program	1,427	-
Interest income	1,207	257
Allowance for funds used during construction	392	774
Other income	564	285
Finance income	174	245
	35,085	29,872
Expenses		
Administration (note 19)	8,263	7,841
Operations and maintenance (note 20)	7,597	6,760
Amortization of property, plant and equipment	5,061	5,140
Amortization of deferred charges and water licensing costs	2,146	948
Interest on long-term debt	1,550	1,229
Provision for uninsured losses (note 11)	150	50
	24,767	21,968
Net income before other items	10,318	7,904
Settlement of lawsuit	-	(3,000)
Rate stabilization/Interim electrical rebate program (note 1)	(2,462)	(2,167)
Unrealized gain (loss) on interest rate swaps (note 25)	1,101	(1,397)
Net income	8,957	1,340
Other comprehensive income	-	-
Comprehensive income	8,957	1,340
Retained earnings, beginning of year	98,276	96,936
Retained earnings, end of year	$ 107,233	$ 98,276

The accompanying notes are an integral part of the financial statements.

Yukon Development Corporation

Consolidated Statement of Cash Flows

For the year ended December 31, (in thousands of dollars)	2009	2008
Operating activities		
Cash receipts from customers	$ 31,614	$ 28,789
Cash paid to employees and suppliers	(20,789)	(15,855)
Interest paid	(1,550)	(1,229)
Interest received	1,381	502
Cash provided by operating activities	**10,656**	12,207
Financing activities		
Repayment of long-term debt	(3,689)	(1,936)
Proceeds from long-term debt	5,000	16,081
Proceeds from construction financing	25,000	-
Contributions in aid of construction	1,180	10,638
Cash provided by (used in) financing activities	**27,491**	24,783
Investing activities		
Addition to property, plant and equipment	(17,859)	(40,819)
Addition to deferred charges	(4,984)	(2,416)
Proceeds from investments	682	583
Proceeds from long-term receivable	495	-
Cash used in investing activities	**(21,666)**	(42,652)
Net increase (decrease) in cash	**16,481**	(5,662)
Cash, beginning of year	**686**	6,348
Cash, end of year	**$ 17,167**	$ 686

The accompanying notes are an integral part of the financial statements.

1. Nature of Operations

Yukon Development Corporation (the "Corporation") was originally established under the *Yukon Development Corporation Act* to participate with the private sector in the economic development of the Yukon, to make strategic investments to the benefit of the territory and to acquire and operate the assets of Northern Canada Power Commission in the Yukon. In 1993, the Corporation's mandate was changed to restrict its new initiatives to energy-related activities designed to promote the economic development of the Yukon.

The Corporation's wholly-owned subsidiary, Yukon Energy Corporation (the "Utility") was incorporated under the *Yukon Business Corporations Act*. The Utility transmits, distributes and sells electrical energy in the Yukon and is subject to overall regulation by the Yukon Utilities Board (YUB) and specific regulation by the Yukon Territory Water Board. Both of these boards are independent from the Utility. The Utility is also exempt from the Financial Administration Act (Yukon).

Rate regulation

The operations of the Utility are regulated by the YUB pursuant to the *Public Utilities Act (Yukon)*. There is no minimum requirement for the Utility to appear before the YUB to review rates. However, the Utility is not permitted to charge any rate for the supply of power that is not approved by an Order of the YUB. The Utility is subject to a cost of service regulatory mechanism under which the YUB establishes the revenues required (i) to recover the forecast operating costs, including depreciation and amortization, of providing the regulated service, and (ii) to provide a fair and reasonable return on utility investment or rate base. As actual operating conditions may vary from forecast, actual returns achieved can differ from approved returns.

The regulatory hearing process used to establish or change rates typically begins when the Utility makes an application for its proposed electricity rate changes over the next one or two forecast years. The YUB must ensure that its decision, which fixes electricity rates, complies with appropriate principals of rate making, all relevant legislation including the *Public Utilities Act* and directives issued by the Yukon Government through Orders-In-Council that specify how the interests of the customer and Utility are to be balanced.

The YUB typically follows a two-stage decision process. In the first stage, the total costs that the Utility will incur to provide electricity to its customers over the immediate future are reviewed and approved. The approval of these costs determines the total revenues the Utility is allowed to collect from its customers. It is the responsibility of the YUB to examine the legitimacy of three classes of costs:

- the costs to the Utility to run its operations and maintain its equipment (personnel and materials);
- the cost associated with the amortization of all capital equipment; and
- the return on rate base (the costs related to borrowing that portion of the rate base which is financed with debt, and the costs to provide a reasonable rate of return on that portion of the rate base which is financed with equity).

As well, in the first stage, the YUB reviews the addition of costs to the rate base and assesses these costs to ensure they are prudent.

In the second stage, the YUB approves how the revenue will be raised. This stage essentially determines the electricity rates for the various customer classes in the Yukon: residential, government, commercial and industrial. This process is guided mainly by requirements of Yukon Government Order-in Council 1995/90 and can include a cost-of-service study which allocates the overall Utility's cost of service to the various customer classes on the basis of appropriate costing principles.

Normally, the Utility applies for rates in advance of the applicable years. The last rate application was filed on October 6, 2008 for the 2008 and 2009 forecast years. The YUB released Order 2009-8 on September 8, 2009. This order gave the Utility direction on certain accounts for the 2008 and 2009 year.

1. Nature of Operations - continued

As the 2008 year was already completed the financial impact of the Order related to the 2008 year was accounted for through the 2009 year. The order resulted in a decrease of $404,000 of net income in the 2009 year.

Water regulation
The Yukon Territory Water Board pursuant to the *Yukon Waters Act* decides if and for how long the Utility will have a water license for the purposes of operating hydro generation stations in the Yukon. The licenses will also indicate terms and conditions for the operation of these facilities.

Capital structure
The Utility's policy is to maintain a capital structure of 60% debt and 40% equity at year end. Annual dividends are declared to the parent and typically loaned back in order to maintain this ratio.

Rate stabilization fund
In May 2008, the Yukon Government authorized the continuation of the Rate Stabilization Fund (the "Fund") for one year at current levels, to July 1, 2009. The Fund provided subsidies to non-government residential, commercial and municipal customers. It was implemented in 1998 after the Faro mine closed to protect customers from significant bill increases that would have resulted from that shutdown. Effective July 1, 2009 the Yukon Government introduced a new rate subsidy program called the Interim Electrical Rebate, which will be in effect until June 30, 2010. The rebate applies to non-government residential and municipal customers. The Yukon Government is providing funding for the Interim Electrical Rebate to a maximum of $3 million. In 2009, the Corporation received $1.427 million in funding for the program. The total subsidy payments made by the Corporation during the current year were $2.462 million (2008 - $2.167 million)

2. Accounting Changes

Rate regulation
Effective January 1, 2009, the Canadian Institute of Chartered Accountants (CICA) has removed the temporary exemption in Section 1100 Generally Accepted Accounting Principles, which provides relief to entities subject to rate regulation from the requirement to apply the section of the recognition and measurement of assets and liabilities arising from rate regulation. Canadian GAAP permits an entity to consult sources other than primary sources of GAAP to assist in selecting accounting policies. In particular, accounting standards published with the authority of the US Financial Accounting Standards Board (FASB). The Utility has consulted FASB and, more specifically, section SFAS 71 in regards to rate regulated accounting and the Utility meets the criteria set out by this section. The Utility will be following SFAS 71 for recording rate regulated assets and liabilities. The CICA continues to give direction on how to disclose rate regulated accounting and the Utility follows this direction. The adoption of this standard did not have an impact on the Utility's financial statements since the recognition standards under SFAS 71 are similar to previous Canadian GAAP.

Goodwill and intangible assets
Effective for years starting on or after October 1, 2008, the CICA has issued Section 3064 Goodwill and Intangible Assets which replaces Sections 3062 Goodwill and Other Intangible Assets and 3450 Research and Development. The new section is in alignment with International Financial Reporting Standards, International Accounting Standard 38 - Intangible Assets (IFRS IAS 38) with respect to the definition and initial recognition criteria of intangible assets, including internally generated intangible assets. Section 3064 reinforces the distinction between costs that should be expensed and those that should be capitalized. As a result of adopting Section 3064, the Utility classified $5,222,000 of deferred water licencing costs as an intangible.

2. Accounting Changes - continued

Credit risk and the fair value of financial assets and financial liabilities
In January 2009, the Emerging Issues Committee (EIC) of the CICA issued EIC Abstract 173 "*Credit Risk and the Fair Value of Financial Assets and Financial Liabilities*" (EIC 173) which requires the consideration of the Corporation's own credit risk and the credit risk of the Corporation's counterparty when determining the fair value of financial assets and liabilities. The adoption of this new section was effective for the Corporation's financial statements for the year ended December 31, 2009 and did not have a significant impact on the Corporation's financial statements.

Financial instruments
In June 2009, the CICA amended Section 3862 "*Financial Instruments - Disclosures*" to include additional disclosure requirements regarding fair value measurements of financial instruments and enhanced liquidity risk disclosures. All financial instruments measured at fair value must be classified in fair value hierarchy levels, which are as follows:
Level 1 - Financial instruments are considered Level 1 when valuation can be based on quoted prices in active markets for identical assets or liabilities.
Level 2 - Level 2 financial instruments are valued using quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or models using inputs that are observable.
Level 3 - Financial instruments are considered level 3 when their fair values are determined using pricing models, discounted cash flow methodologies or similar techniques and at least one significant model assumption or input is unobservable.

Liquidity risk disclosure was also enhanced with the inclusion of a maturity analysis for derivative and non-derivative financial liabilities. The amendments were effective for the Corporation's financial statements for the year ended December 31, 2009. To provide relief for financial statement preparers, the CICA decided that comparative financial information for the new disclosures was not required in the first year of application. As the amendments only concern disclosure requirements, they do not have an impact on the results or financial position of the Corporation. The required disclosures are included in note 25.

3. Significant accounting policies

Financial statement presentation
The consolidated financial statements of the Corporation have been prepared by management in accordance with Canadian generally accepted accounting principles ("GAAP") and include the accounts of Yukon Development Corporation and its wholly owned subsidiary, Yukon Energy Corporation. All significant inter-company transactions and balances have been eliminated on consolidation. The consolidated financial statements also reflect the regulatory policies adopted by the Utility which differ from the accounting policies otherwise expected using GAAP. In particular, the timing of the Utility's recognition of certain assets, liabilities, revenues and expenses as a result of regulation differ from that of a non-regulated enterprise. Impacts of accounting for rate regulated operations are further described in note 4. Consequently, the significant accounting policies have been classified accordingly in the notes below:

Rate regulated accounting policies adopted by the Utility

Property, plant and equipment
The Utility capitalizes an allowance for funds used during construction ("AFUDC") calculated at the weighted average cost of capital which was 7.61% for 2009 (2008 - 7.61%). Upon retirement or disposal any gain or loss is charged to income in the current year for assets amortized on an individual basis, or charged to accumulated amortization for assets amortized on a pooled basis.

3. **Significant accounting policies - continued**

Faro Mine dewatering deferral revenue
Faro mine dewatering deferral revenue represents amounts ordered by the YUB to be held by the Utility on behalf of ratepayers. Typically these amounts are either refunded to the customers or applied to ratepayer deficits through the ratesetting process or through YUB orders.

Deferred uninsured losses
The Utility maintains a regulatory account for recording uninsured losses. An annual provision is approved by the YUB and collected through customer rates. Variances between the approved annual provision and actual costs incurred are deferred until the following general rate application or until a specific application is made to the YUB requesting recovery from or refund to customers.

Deferred charges
Deferred charges are recorded at cost less accumulated amortization.

All deferred charges are amortized to earnings on a straight-line basis over terms approved by the Yukon Utilities Board.

Cost of feasibility studies and infrastructure planning which did not result in a capital project are amortized over terms raging between five and ten years.

Deferred customer service costs are amortized over twelve years.

The deferred hearing cost account is used to record the deferral of costs associated with preparation and defense of applications to the YUB. The periods of amortization range from 2 to 45 years.

Regulatory provision for future removal and site restoration costs
The Utility maintains a provision for the future removal of property, plant and equipment and the costs of site restoration related to those assets. Per YUB Order 2005-12 no additional provision is permitted.
This account provides for the costs of demolishing, dismantling, tearing down, or otherwise disposing of an asset and any site restoration costs, net of actual recoveries. This account is not used when the costs relate to an asset retirement obligation.

Deferred insurance proceeds
Deferred insurance proceeds represents a gain on fire insurance proceeds received related to a fire at the Whitehorse Rapids Generating Station in 1997. The proceeds are being amortized to income on the same basis as the replacement assets.

Diesel contingency fund
The Utility maintains an asset and an offsetting liability on behalf of ratepayers. The fund is used to reimburse the Utility for costs associated with diesel generation required when there is not sufficient water for hydraulic generation to meet demand. The Utility is required to file an annual report with the YUB on the fund's activity.

Generally Accepted Accounting Principles ("GAAP") adopted by the Corporation and Utility

Revenue recognition
All revenues are recognized in the period earned. Revenue from the sale of power is recognized based on cyclical meter readings. Sales of power includes an accrual for electricity deliveries not yet billed.

3. **Significant accounting policies - continued**

Materials and supplies
Diesel fuel, materials and supplies are recorded at the lesser of average cost and net realizable value. Obsolete materials and supplies are recorded at salvage value in the period when obsolescence is determined. Major spare parts are recorded in the Utility's books as property and equipment.

Property, plant and equipment
Property, plant and equipment is stated at cost, other than the AFUDC component which is recorded under rate regulated accounting. Cost includes materials, direct labour, a proportionate share of directly attributable administration overhead, and finance charges capitalized during construction, less accumulated amortization. Amortization is based on the straight-line method over the estimated economic life of the assets as follows:

Generation	
Hydro-electric plants	30 to 65 years
Diesel plants	25 to 45 years
Wind turbines	30 years
Transmission	40 to 50 years
Distribution	30 to 40 years
Buildings	20 to 40 years
Financial Information System	5 to 10 years
Transportation	9 to 31 years
Other equipment	5 to 20 years

Asset retirement obligations
On an annual basis the Utility identifies legal obligations associated with the retirement of tangible long-lived assets. Where a reasonable estimate of the fair value of these obligations can be determined, the total retirement costs are to be recorded as a liability at fair value, with a corresponding increase to property, plant and equipment.

The Utility has determined that it has tangible long lived assets with associated future legal obligations for retirement. As the Utility anticipates using the assets for an indefinite period, the date of removal of these assets cannot be reasonably determined, and therefore an asset retirement obligation has not been recorded. When the timing and amount of the retirement can be reasonably estimated, an asset retirement obligation and the corresponding increase in property, plant and equipment asset will be recognized.

Direct financing leases
Investments in direct finance leases are carried at the lower of cost and net realizable value.

Contributions in aid of construction
Certain property, plant and equipment additions are made with the assistance of cash contributions from customers or Government. These contributions are deferred upon receipt and are amortized to income on the same basis as the assets to which they relate. Amortization of contributions from customers is netted on the statement of operations against amortization expense.

Deferred water licensing costs
Costs related to obtaining water license renewals are deferred and amortized to earnings on a straight line basis over the term of the license. The Utility operates its hydro generation facilities under three separate water licenses, with terms ranging from 17 to 25 years. These costs are treated as intangible assets and are measured at initial cost and amortized over the life of the water license.

3. **Significant accounting policies - continued**

Employee pension plan
The Utility has a defined benefit pension plan which provides for pensions based on length of service and final average earnings. Employees joining the Utility after January 1, 2002 are not eligible to participate in the defined benefit plan. The cost of pension benefits is actuarially determined using the projected benefits method, prorated on service, and reflects management's best estimates of investment returns, wage and salary increases, and age at retirement. Adjustments resulting from plan enhancements, actuarial gains and losses, and changes in assumptions are amortized over the expected average remaining service period of active employees. Pension costs include the current cost of service, amortization of past service benefits and plan enhancements, and actuarial gains and losses. Unrecognized gains and losses are amortized on a straight-line basis over the expected average remaining service period of active employees, which is currently 12 years. The transitional asset that arose when this policy was first applied is amortized over the average remaining service period of active employees expected to receive benefits under the benefit plan as of January 1, 2000. The expected return on plan assets is based on the fair value of these assets.

Financial instruments
Financial assets and financial liabilities are recognized on the Corporation's balance sheet when the Corporation becomes party to the contractual provisions of the instrument.

Cash
Cash is comprised of cash on hand and in bank accounts.

Accounts receivable and long-term receivable
Accounts receivable and the long-term receivable, classified as loans and receivables, are initially measured at fair value. Subsequent to initial recognition, accounts receivable and the long-term receivable are measured at amortized cost less any impairment.

Accounts payable and accrued liabilities
Accounts payable and accrued liabilities, classified as other financial liabilities, are measured at amortized cost.

Short and long-term debt
Short and long-term debt, classified as other financial liabilities, are initially recognized at fair value. Subsequent to initial recognition, short and long-term debt is measured at amortized cost.

Derivative financial instruments
Derivative financial instruments are financial contracts that derive their value from changes in an underlying variable. The Corporation has entered into interest rate swaps to manage interest rate risk. The Corporation's interest rate swaps are designated as held for trading and are thus recognized at fair value on the date the contract has been entered into with any subsequent unrealized gains and losses reported in net income during the period in which the fair value movement occurred.

Fair value estimation
The carrying value of the accounts receivable, accounts payable and accrued liabilities approximate their fair value due to the immediate or short-term maturity of these financial instruments. The fair value of the long-term receivable and the long-term debt is estimated by discounting the future cash flows using current rates for financial instruments subject to similar risks and maturities. The fair value of derivative financial instruments is estimated using standard market valuation techniques and is provided to the Corporation by the financial institution that is the counterparty to the transactions.

3. Significant accounting policies - continued

Environmental liabilities

Environmental liabilities consist of the estimated costs related to the remediation of environmentally contaminated sites. The Utility will accrue a liability and record an expense, related to present or past activities of the Utility, when there is a legal obligation to remediate the contamination and the costs can be reasonably estimated. If the likelihood of the Utility's obligation to incur these costs is either not determinable or the costs cannot be reasonably estimated, the contingency is disclosed in the notes to the financial statements. The Corporation reviews its estimates of future environmental liabilities on an ongoing basis as described in Note 24.

Measurement uncertainty

The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The most significant estimates include those for revenue, accounts receivable, property, plant and equipment, asset retirement obligations, employee pension obligations and regulated assets and liabilities. Actual results could differ by a significant amount from these estimates.

Management's estimates and assumptions, especially those affecting the reported amounts of regulated assets and the Utility's ability to recover the cost of these assets through future rates, are subject to decisions of the YUB as described in note 4.

Future accounting changes

On February 13, 2008 the Canadian Accounting Standards Board confirmed the adoption of International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB) in place of Canadian Generally Accepted Accounting Principles (GAAP) effective January 1, 2011. The Corporation and the Utility are required to present their first set of published IFRS statements for the year ended December 31, 2011 with comparative information. Although IFRS uses a conceptual framework similar to Canadian GAAP, there are differences in accounting standards and the Corporation and the Utility are currently assessing the impact of those differences.

As a first time adopter of IFRS, the Corporation is required to apply IFRS 1 "First Time adoption of International Financial Reporting Standards". A number of exemptions are available under this Standard which the Corporation is currently evaluating. The more significant exemptions include: recognizing through opening retained earnings all cumulative actuarial gains and losses on employee benefit plans, electing to use fair value at the transition date as deemed cost for capital assets in certain circumstances and the opportunity to apply decommissioning liabilities prospectively.

To facilitate the conversion process, the Corporation has appointed an external advisor and assembled a core project team. Project planning started with a high level diagnostic review of significant differences between IFRS and Canadian GAAP. The second phase of the plan is the detailed analysis and design. This phase involves the detailed assessment, from an accounting, reporting and business perspective of the changes that will be caused by the conversion to IFRS. While all the effects of IFRS have not been fully determined, the Corporation has identified a number of key areas where it is likely to be impacted by changes in accounting policy. Areas with significant differences that will impact the Utility include: regulatory accounting, property, plant & equipment, employee benefits, impairment of assets and the overall presentation of the financial statements.

4. Financial statement effects of rate regulation

Certain items in these consolidated financial statements are accounted for differently than they would be in the absence of rate regulation.

Where regulatory decisions dictate, the Utility defers certain costs or revenues as assets or liabilities on the balance sheet and records them as expenses or revenues on the statement of operations as it collects or refunds amounts through future customer rates. Any adjustments to these deferred amounts are recognized in income in the period that the YUB renders a subsequent decision. Regulatory assets represent future revenues associated with certain costs, incurred in the current period or in prior periods, which are expected to be recovered from customers in future periods through the rate-setting process. Regulatory liabilities represent future reductions or limitations of increases in revenues associated with amounts that are expected to be refunded to customers as a result of the rate-setting process.

In the absence of rate regulation the Utility's net income would have decreased by $4,199,000 in 2009 (2008 - decreased by $3,016,000). The following describes each of the circumstances in which rate regulation affects the accounting for a transaction or event:

	2009	2008	Expected remaining recovery/ settlement (years)	For 2009 In the absence of Rate Regulation the Utility's Net Income would have increased (decreased) by:
Regulatory assets				
Deferred charges (note 12), net book value				
Feasibility studies and infrastructure planning	$ 6,455	$ 2,943	5 to 10	$ (3,512)
Deferred customer service costs	700	764	11	64
Hearing costs	1,074	1,348	2 to 45	274
Dam safety review	-	13	0	13
Deferred uninsured losses (note 11)	111	556	Indeterminate	32
Diesel contingency fund (note 10)	887	883	Indeterminate	(4)
	9,227	6,507		(3,133)
Regulatory liabilities:				
Faro Mine dewatering deferral revenue (note 15)	397	1,191	Indeterminate	(381)
Deferred insurance proceeds (note 17)	7,086	7,356	26	(270)
Regulatory provision for future removal and site restoration costs	5,008	5,168	Indeterminate	(160)
Diesel contingency fund (note 10)	887	883	Indeterminate	4
	13,378	14,598		(807)
Net impact of assets and liabilities	$ (4,151)	$ (8,091)		$ (3,940)
Impact of other items through income statement				
AFUDC				(392)
Fuel Price Adjustment				133
Total effect				(4,199)

Regulatory assets

(a) Deferred charges

Deferred charges represent costs which have been deferred and are being amortized over various periods. In the absence of rate regulation, GAAP would require such costs to be recognized as expenses in the year incurred.